

SENATE BILL REPORT

SSB 6785

As of Second Reading, March 14, 2002

Title: An act relating to eliminating Washington estate tax on estates below the federal estate tax liability filing threshold.

Brief Description: Eliminating Washington estate tax on estates below the federal estate tax liability filing threshold.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Snyder, Brown, Poulsen, Rasmussen and Roach).

Brief History:

Committee Activity: Ways & Means: 2/25/02, 3/4/02 [DPS, DNP].

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Substitute Senate Bill No. 6785 be substituted therefor, and the substitute bill do pass.

Signed by Senators Brown, Chair; Regala, Vice Chair; Fairley, Vice Chair; Fraser, Kohl-Welles, Long, Poulsen, Rasmussen, Rossi, B. Sheldon, Snyder, Spanel, Thibaudeau and Zarelli.

Minority Report: Do not pass.

Signed by Senator Sheahan.

Staff: Terry Wilson (786-7433)

Background: The federal government imposes a tax on the transfer of property at death. This tax is known as the federal estate tax. The state of Washington imposes a tax on the transfer of property at death which is equal to the amount of tax authorized as a credit against the federal estate tax for state taxes. The federal estate tax was changed substantially by the Economic Growth and Tax Relief Reconciliation Act of 2001 (the "Federal Act"), which took effect June 7, 2001.

The Federal Law Prior to Adoption of the Federal Act. Under prior law, the federal estate tax was imposed at graduated rates ranging from 18 percent for taxable estates under \$10,000 to 55 percent for estates over \$3 million. An additional tax was imposed equal to 5 percent on taxable estates between \$10 million and an amount where the average tax rate equals 55 percent. This effectively phased out the graduated rate structure.

A unified credit was available to every person which was applied to taxes on gifts made during a person's lifetime and to taxes on transfers at death. The effect of the unified credit was to exempt estates below \$700,000 (or \$1,400,000 for a community property couple) for calendar year 2002. The unified credit was scheduled to increase to the equivalent of an exemption of \$1,000,000 (or \$2,000,000 for a community property couple) by 2006.

Another credit was available against the federal estate tax equal to inheritance or estate taxes paid to the state. The federal credit for state taxes is limited statutorily according to a formula based on the size of the estate. The federal law allows an exclusion of \$60,000 in determining an adjusted taxable estate for purposes of computing the state credit. The actual amount of the credit is determined by a schedule which ranges from 0.8 percent for taxable estates between \$40,000 - \$90,000, up to 16 percent for taxable estates valued in excess of \$10,040,000.

The Federal Law After Adoption of the Federal Act. The Federal Act phases out the federal estate tax by 2010. It does this by:

- (1) Eliminating the 5 percent surtax and immediately reducing the top tax rate from 55 percent to 50 percent in 2002 and then reducing the top tax rate by 1 percent per year down to 45 percent in 2007.
- (2) Increasing the unified credit to the equivalent of an exemption of \$1.0 million in 2002, \$1.5 million in 2004, \$2.0 million in 2006, and \$3.5 million in 2009.
- (3) Reducing the federal credit for state taxes by 25 percent in 2002, 50 percent in 2003, and 75 percent in 2004. Beginning in 2005, the credit for state taxes is eliminated. However, a deduction from the value of the federal taxable estate is allowed for the amount of any estate taxes paid to the state.

For calendar year 2010, the federal estate tax is repealed. However, the Federal Act sunsets December 31, 2010, and the federal estate tax is re-established as it existed before the Federal Act for calendar year 2011 and thereafter.

Requirement for Legislative Action to Adopt Federal Changes in the Estate Tax. The Washington estate tax refers to the Internal Revenue Code as it exists on January 1, 2001. This makes it necessary for the Legislature to adopt a conforming amendment to incorporate any changes in the federal Internal Revenue Code. Most states impose an estate tax equal to the federal credit. Nine states are considering legislation to retain some type of estate tax.

Summary of Bill: The changes in the federal estate tax are incorporated into the Washington estate tax, except the four-year phase out of the federal credit for state taxes is not incorporated. This effectively phases out the state tax by 2010 with the federal tax.

The act applies to decedents dying on or after January 1, 2002.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect immediately.

Testimony For: None.

Testimony Against: This bill will cause undue hardship on small business. It is unwise to penalize small business owners and farmers who will be forced to sell their property.

Testified: CON: Michael Carrico, Estate Planning Council of Seattle; Mark Johnson, NFIB.